

Before the
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In The Matter of)
)
Review of Regulatory Requirements) CC Docket No. 01-337
For Incumbent LEC Broadband)
Telecommunications Services)

COMMENTS OF SPRINT CORPORATION

Sprint Corporation, on behalf of its incumbent LEC, competitive LEC, long distance, and wireless divisions, in response to the Notice of Proposed Rulemaking (NPRM) released December 20, 2001 (FCC 01-360), hereby respectfully submits its comments in the above-captioned proceeding.

I. INTRODUCTION AND SUMMARY

In this NPRM the Commission seeks comments on what "regulatory safeguards and carrier obligations, if any, should apply when a carrier that is dominant in the provision of traditional local exchange and exchange access services provides broadband service."¹ The Commission has also requested comment on SBC Communication's October 3, 2001 Petition for an expedited ruling that it is non-dominant in the provision of broadband services.²

¹ NPRM at para. 1.

² *Id.*, at para. 7. Additionally, there are two pending proceedings that could impact, or be impacted by, the ultimate outcome of this proceeding: *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, CC Docket No. 01-318, NPRM, released November 19, 2001; and *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, CC Docket No. 02-33, NPRM, released February 15, 2002.

Sprint believes that the Commission's traditional view that telecommunications services should be divided between a mass market product market and a larger business product market should apply to broadband services. There is a clear distinction between the services provided these two groups; a distinction that does not easily allow for interchangeability between the services.

It is also evident that in the mass market product market there is sufficient intermodal and intramodal competition to demonstrate that the ILECs do not have significant market power in the provision of broadband services. However, complete regulatory relief cannot be granted. The ILECs continue to maintain bottleneck control over the facilities necessary to provide intramodal competition and thus while some degree of pricing flexibility and tariff filing relief may be warranted, the ILECs must continue to be subject to regulation, specifically to Sections 251 and 252 of the Telecommunications Act.³

Likewise, in the larger business product market there appears to be sufficient intramodal competition, but not intermodal, to allow some pricing flexibility and tariff filing relief for the ILECs. However, due to the ILECs' bottleneck control of the necessary facilities, the continued existence of this intramodal competition is dependent upon continuing the ILECs' resale and UNE obligations under Sections 251 and 252.⁴

II. RELEVANT PRODUCT MARKET

In the instant NPRM, the Commission seeks comment on how to define the appropriate product market that includes ILEC broadband services. Specifically, the Commission requests input regarding the bifurcation of the broadband market into two

³ 47 U.S.C. § 251 and 47 U.S.C. § 252.

⁴ *Id.*

distinct markets: the *mass market* broadband market and the *large business* broadband market.⁵

Economists have long held that a “market” is the set of buyers and sellers whose activities have an effect on the price of a product or service.⁶ As such, a market is not limited to the supply and demand of any single product but it includes the supply and demand of other products that act as forces on the price of the first. In the case of broadband services, if one service is generally considered a substitute for another, then the two services could be said to operate in the same market. This concept of substitutability is actually key to understanding the proposed bifurcation raised in the NPRM: to the extent that substitutability generally exists *within* the two proposed markets, but not *across* the two markets, the separation is reasonable.

The standard of substitutability often used in anti-trust situations involves the concept of *reasonable interchangeability of use*.⁷ Reasonable interchangeability of use does not require that two products be functionally equivalent, only that they satisfy a similar customer demand. It also allows for quality differences among goods and services.

It is clear that many of the services offered in the *mass market* broadband market—xDSL, cable modems, satellite, fixed wireless—are designed to meet the same customer needs, primarily high-speed internet access and (to a lesser degree) remote access for work-at-home applications.⁸ It is also clear that these needs are very different

⁵ NPRM at para. 20.

⁶ Baumol and Blinder, *Economics*, Harcourt Brace Jovanovich, 1979.

⁷ *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962).

⁸ The Commission has requested comment on potential intermodal competition offered by the mobile wireless market. While it is clear that the mobile wireless market, including Sprint PCS, is making significant strides toward providing higher-speed services and applications to the mass market, at this point in time it is premature to make assumptions regarding whether these services will be viewed as *substitutes*

from the needs met by many services offered in the *large business* market: LAN-to-LAN connections, server to server connections, high-capacity backbones for company intranets. It is true that there are instances where the two markets overlap: a small-to-medium business customer could easily view xDSL as a substitute for a remote-to-host connection provided by frame relay, or conversely a small business could purchase a DSL line solely to provide high-speed internet access identical to that purchased by a residential customer. But these areas of overlap represent the exception, rather than the rule.

This exception does not rise to the level of demonstrating interchangeability of broadband services between the mass market and the larger business market. Nor does the exception rise to the level of an additional product market for small-to-medium business customers. Rather, the rule bears out that there are two relevant product markets: mass market broadband and larger business broadband markets.

III. MARKET POWER

In the instant NPRM, the Commission asks for comment as to whether incumbent LECs possess market power in the provision of broadband services.⁹ Having established that it is appropriate to bifurcate the overall broadband market into *mass market* broadband and *large business* broadband, Sprint believes it is also correct to address questions of market power with regard to each product market separately, and does so below. However, for the sake of accuracy it is necessary to clarify the definition of “market power” in this context.

or *complements* to wireline products. As such, the controlling effect that these services may or may not have on market power of wireline providers is impossible to determine.

⁹ NPRM at para. 28.

Traditional textbook definitions emphasize *prices in excess of an appropriate cost measure* as evidence of market power, and so are consistent with the Commission's discussion that defines market power as the ability to "raise and sustain prices" by restricting output (a firm's own, or a rival's) or by raising rivals' costs.¹⁰ But in the context of examining the possibility of reduced regulation or de-regulation of broadband services, it is appropriate to expand the issue at hand to address *monopoly power* as well. Monopoly power is "the ability of individuals or firms currently in business to prevent other individuals or firms from entering the same kind of business."¹¹ Although the two terms are often used interchangeably, it is clear that in many cases a firm's market power is derived from its monopoly power.¹²

The Commission has long acknowledged that the economies of scale inherent in the public switched telephone network have the effect of creating a barrier to entry for many potential competitors.¹³ These same economies of scale characterize the provision of wireline-based broadband service, and create just as effective a barrier to entry in many cases. Because the ILEC possesses these economies as a direct result of government-mandated monopoly status, if competitors were not able to avail themselves of the same economies through unbundling and resale, then the ILEC could be said to

¹⁰ NPRM at para 28. See also, for example, Browning and Zupan, Microeconomic Theory and Application (Sixth Edition), Addison-Wesley, 1999.

¹¹ David C. Colander, Economics, Irwin Publishers, Second Edition, 1995.

¹² Because of the technological constraints that characterize wireline broadband deployment, the first type of market power referred to in the NPRM (a firm's ability to raise prices by restricting its *own* output) is a non-issue for the mass market broadband market. The concept of increasing prices (or profits) by reducing output assumes that only enough of a product is provided so that a subset of customers—those willing to buy at a higher price—actually receives the good. The physical deployment of broadband makes it impossible to provide service only to those customers in a subdivision or in a wire center who are willing to pay a higher price.

¹³ *In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, FCC 99-238, released November 5, 1999 ("*UNE Remand Order*").

possess monopoly power; the costs faced by any potential rival would create an economic burden that would preclude entry into the market.¹⁴ (It is worth noting that the ILEC's chief competitor in the *mass market* broadband market, the cable television company, also possesses entry-inhibiting economies of scale as a result of a government-mandated monopoly and so equally enjoys monopoly power with, currently, freedom from regulation.¹⁵) However, currently competitors are able to avail themselves of these economies because of ILEC unbundling, collocation, and resale obligations.

The Commission has also clearly established its interest in intermodal competition, and has recognized that intermodal competition can reduce the likelihood of anti-competitive behavior.¹⁶ Sprint welcomes this opportunity to clarify one aspect of the Commission's point: Intermodal competition can (in some cases) reduce the likelihood of anticompetitive behavior with regard to *pricing of output*, but not with regard to other forms of anticompetitive behavior. The economies of scale enjoyed by ILECs that could potentially preclude the introduction of intramodal competition are not affected by the existence of intermodal competition. But intermodal competition can reduce the likelihood of anti-competitive behavior when there is perceived substitutability among

¹⁴ The actual conditions and circumstances in which a competitor would not be able to replicate the necessary economies of scale will vary from market to market, due to factors such as geographic layout of customers. They will also vary depending on which portions of the network exhibit the needed economies. These various conditions and circumstances will be addressed at length in Sprint's forthcoming comments in the UNE triennial review.

¹⁵ Whether the absence of cable modem regulation should be continued is also the subject of a pending Commission proceeding. The issue of how cable modem service should be classified (and regulated or not) is the subject of *Inquiry Concerning High-Speed Access to the Internet over Cable and Other Facilities*, GN Docket No. 00-185, Notice of Inquiry, 15 FCC Rcd 19287 (2000) (Cable Access Notice) The outcome is critical to the efficacy of the outcome of this docket. Sprint urges the Commission to resolve the Cable Access Notice and the instant proceeding so as to ensure intermodal competitive neutrality, as well as, continuing ILEC UNE, Collocation, and resale obligations to ensure intramodal competitive neutrality.

¹⁶ NPRM paragraph 30.

services on the part of the end-user.¹⁷ And the *extent* to which intermodal competition can control prices depends on how perfectly the substitutability is perceived by customers; if customers perceive there to be significant *product differentiation* among services then the ability of one service to control the price of the other is greatly reduced.¹⁸

In the case of intermodal competition for mass market broadband services such as xDSL and cable modems, it is obvious that the two are often viewed as substitutes by consumers. This is supported by the fact that advertising in popular media aggressively attempts to emphasize *differences* in the products—when customers already view products as differentiated, firms do not need to spend large amounts pointing out the differences to potential buyers.¹⁹ Therefore it is apparent that even if intermodal competition in the mass market broadband market does not control potential *monopoly* power that ILECs possess, it is somewhat effective at controlling any *market* power the ILECs possess in many cases.

With regard to *large business* broadband, the situation is similar. A service such as frame relay may be provided by an ILEC, a CLEC or an IXC, but in many cases competition can only act as a controlling force on prices because the underlying network asset is available to competitors. As long as this is the case, market power (defined as an ability to raise and sustain prices above competitive levels) is controlled because monopoly power is controlled, and monopoly power is controlled by the availability of network elements.

¹⁷ Indeed, the specific cite reference made in the NPRM taken from Comsat's Petition for Forbearance explicitly refers to this substitutability (NPRM footnote 72).

¹⁸ Browning and Zupan, Microeconomic Theory and Application, Chapter 12.

¹⁹ To turn to a non-telecom example, one sees precious little advertising touting the benefits of a luxury auto over an economy car.

IV. ALTERNATIVE REQUIREMENT

The instant NPRM asks for comment on “alternative requirements” for these broadband services, including de-regulation or reduced regulation.²⁰ At this point in time it is clear that, while the Commission would be premature in declaring any ILEC non-dominant in the provision of broadband services and essentially de-regulating the services, the existence of intermodal competition and the potential for intramodal competition provide justification for the Commission to examine increased pricing and tariff filing flexibility at the retail level. While Sprint cannot comment on any ILEC serving territory other than its own, it is clear that, in Sprint’s local serving territory, these conditions—intermodal competition and availability of network assets—create a situation in which it is likely that prices will successfully be controlled by market forces.²¹ Therefore increased pricing and tariff filing flexibility is in order.

However, this increased flexibility is dependent upon continuing the ILECs' Section 251 UNE, collocation, and resale obligations. Sprint agrees with the Commission that the continued existence and enforcement of these Section 251 obligations reduce the need for complete dominant carrier regulation through the grant of increased pricing and tariff filing flexibility.²²

²⁰ NPRM at para. 33.

²¹ Sprint estimates that in excess of 113,000 cable modems are in place in Sprint ILECs' territories, representing approximately twice the number of residential DSL lines that Sprint has provisioned. This estimate is based on estimated cable network upgrades and projections of national penetration by cable providers.

²² NPRM at para. 44.

V. CONCLUSION

The broadband services market should be divided into two relevant product markets -- mass market and larger business. In both of these markets there is a demonstration of existing competition that justifies some degree of pricing flexibility and tariff filing flexibility, but only if the ILEC Section 251 UNE, collocation, and resale obligations continue.

Respectfully submitted,

SPRINT CORPORATION

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